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(U) CHINA'S HIGHWAYS AND VEHICLE INDUSTRY: A ROAD TO EVERY VILLAGE, A TRUCK IN EVERY BARN?

Summary

China has embarked on a costly, long-term program to develop its small and backward highway system in an effort to improve commercial and cultural linkages and relieve strain on its over-burdened railways. A variety of innovations in pricing, incentives, industrial organization, and allocation of responsibility for construction has already resulted in a boom in the auto industry which is likely to continue into the next decade and beyond.

Even planned increases in production, however, cannot be expected to keep up with demand. In the last year, to help meet the mushrooming demand, China's vehicle imports have jumped dramatically and the process of purchasing a vehicle has been streamlined somewhat. Shortages and long delivery delays, however, have given rise to a growing problem of shady and illegal deals and massive smuggling.

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China's Underdeveloped Road System

China's road system has long suffered from lack of coordination, inattention, and under-investment; consequently it remains small and underdeveloped. China has only about 930,000 kilometers of all types of roads, less than Japan, Brazil, or the USSR and only about one-sixth as much as the US. Highways are relatively lightly used owing to the small number of vehicles and the inefficiency of state-owned transport companies. For example, railroad mileage is only about

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5.6 percent of highways mileage (about 50,500 km), but the highways carry less than 5 percent of the freight volume transported by rail--in 1984, 35.9 billion ton/km by road compared with more than 724 billion ton/km by rail.

Put another way, almost half of China's overall freight traffic volume travels by rail, but only slightly more than 2.4 percent by road. In addition, despite the heavy passenger load carried by urban mass transit, highways move only about three times as many people per year as trains.

The causes of China's highway underdevelopment are many, but lack of central coordination and low investment priority are among the most important. The Ministry of Communications is nominally in charge of China's highways but in reality controls policy only over major trunk roads. Local road development is up to local authorities, which in practice means neglect. In recent years, less than 2 percent of the state capital construction budget has been allocated to highway development, or less than one-third the amount spent on railroads. One feature of the Seventh Five-Year Plan, however, is reportedly a vehicle tax to raise revenue for road construction.

Highway Development Plans

China now is undertaking measures to improve its highway system. The government is said to have plans to build an additional 96,000 kilometers of rural roads by 1987 to smooth the flow of agricultural produce to the cities and the transport of fertilizer and consumer goods to the countryside. The Chinese also plan to build or upgrade 114,000 kilometers of trunk roads during this period. In 1984, some 15,000 kilometers of roads were constructed, reportedly nearly double the 1983 total, and more than 29,000 kilometers were rebuilt or widened. The central government allegedly has earmarked an additional 2.8 billion yuan (about $1 billion) worth of grain, cotton, and cloth, about 60 percent of which will be used to pay corvee laborers working on rural road construction.

Highway development policy entails a number of structural and incentive changes. Recently, for example, the State Council implemented plans to raise freight-rate charges for short-distance rail transport in an effort to encourage the development of local trucking and shipping companies.

China's Vehicle Industry Boom

Reinforcing plans to develop the highway system is a program to increase dramatically vehicle production and to ease the procedures for buying vehicles. The auto industry in 1982 underwent

a major reorganization designed to promote tighter planning and coordination, specialization, technical upgrading, management reform, and competition. The new China Automotive Industry Corporation--composed of the 37 most important vehicle plants and about 2,000 parts and accessories factories--plans to increase output at an annual rate of 8.6 percent through the mid-1990s and to accelerate to more than 9-percent growth in the following decade.

Vehicle plants are already off to a good start in boosting production. In 1984, China built more than 300,000 vehicles--the industry's capacity and a 27-percent increase over 1983. This year, the automotive industry plans to produce 363,000 vehicles. A number of joint ventures and licensing agreements have been signed to upgrade technical standards, including joint ventures with the US Jeep company and with Volkswagen, and discussions are under way for other joint ventures and licenses.

Demand, however, continues to outpace supply, particularly in the rural areas where the responsibility system has created both increased need for transport and greater availability of funds. According to a recent State Council decision, some 76,500 vehicles will be sold in the countryside next year. About 70 percent of these will be sold to peasant cooperatives for farm work and transport, with the remainder going to individuals.

Demand for Vehicles Creates Problems

Even increased production, however, cannot keep up with demand, and China has been buying large quantities of vehicles, especially from Japan. Last year China is said to have imported more than 100,000 vehicles, of which some 20,640 were Japanese trucks, up from 3,750 in 1983. Passenger cars--China produces only about 5,000 per year--are in particularly high demand with the number of imported Japanese cars alone jumping from fewer than 3,200 in 1983 to almost 49,000 in 1984. Industry officials, according to one Western press report, estimate that China will need 600,000 new vehicles every year to meet demand between now and the year 2000.

The boom time for China's vehicle industry, however, has created a number of problems. According to a recent Hong Kong press report, the China Automotive Industry Corporation is concerned that a headlong rush to develop vehicle production is leading to loss of coordination. New vehicle factories are springing up--25 in 1984 alone--and competition for technology transfer agreements with foreign companies is creating chaos and driving up the cost of such arrangements. In addition, according to the report, imports of both finished vehicles and parts for assembly have grown out of control.

Perhaps a more serious problem, however, is the dramatic increase in "back door" and illegal schemes for matching supply and demand. In recent months, China has opened six regional auto "showrooms" at which customers can order domestic or foreign-made vehicles. Generally no floor samples are available, terms are cash up-front, and delivery times average about six months. In addition, buyers must arrange for pickup at dockside, sometimes on the other side of the country. Prices seem to range from about $40,000 up. Nevertheless, business is said to be brisk.

Under such conditions, it is not surprising that entrepreneurs have leapt into the breach. Hainan, utilizing its government-granted import authority, is said to be at the center of a massive national smuggling ring. According to a well-connected Hong Kong journal, the Hainan government has approved import licenses for 50,000 automobiles, most of them destined for the interior in illegal deals. These activities prompted a crack-down by provincial and central authorities and a public apology by Hainan officials. But until supply approaches demand, would-be vehicle purchasers are likely to continue to seek ways to evade the lengthy and uncertain process of buying through state channels.

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